

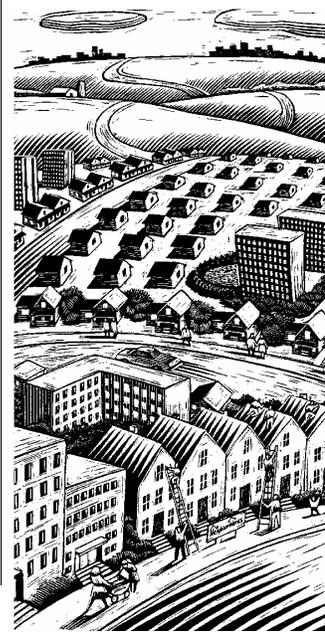
Written Testimony of
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*Promoting the American Dream of
Homeownership through Down Payment
Assistance*

Submitted to the U.S. House of Representatives
Committee on Financial Services
Subcommittee on Housing and
Community Opportunity

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Good afternoon, Subcommittee Chairman Ney, Ranking Member Waters, and members of the subcommittee. My name is Lori Gay and I am the executive director of Los Angeles Neighborhood Housing Services (LA NHS). I have worked in the community development field for the past 18 years, and have focused my efforts on rebuilding impoverished communities and creating mechanisms for resident empowerment and expanding homeownership opportunities for low- and moderate-income families – with a particular emphasis on serving new immigrants and minority families. I am here this afternoon to talk with you about the benefits of downpayment assistance for low- to moderate-income borrowers based on the experience of the LA NHS.

Los Angeles Neighborhood Housing Services

Let me first say a word about the LA NHS, where I have worked since 1990. Over the last 13 years, LA NHS has served over 1.4 million families, developed and rehabilitated over 6,200 housing and commercial units, established 150 block clubs, educated and counseled over 68,000 prospective home buyers, and employed over 200 neighborhood youth, while investing more than \$1.1 billion back into some of Los Angeles' toughest neighborhoods. I am proud to report that LA NHS is the largest, comprehensive provider of affordable homeownership in Southern California, putting 38 families a day on the road to homeownership.

I also serve as Chair, California Organized Investment Network (COIN), Board Member, Federal Reserve Bank of San Francisco--Los Angeles Branch, The Gas Company--Consumer Advisory Council Member, and Washington Mutual Community Advisory Council Member.

Member of the NeighborWorks Network

Los Angeles Neighborhood Housing Services is a member of the NeighborWorks[®] network -- founded and supported by Neighborhood Reinvestment Corporation. The Neighborhood Reinvestment Corporation strengthens communities and transforms lives across America by supporting innovative local partnerships of residents, businesses, and government, collectively known as the NeighborWorks[®] network, and by advancing broader community development goals. This year alone, the NeighborWorks[®] system will generate nearly \$2 billion of direct investment in more than 2,300 lower-income urban, suburban and rural communities nationwide; help more than 38,000 lower-income families purchase, improve and maintain their homes; provide pre-purchase and post-purchase homebuyer counseling to more than 78,000 families. NeighborWorks[®] organizations also own and managed over 36,000 rental or mutual housing units

LA NHS and each locally governed NeighborWorks[®] organization operates a revolving loan fund for non-conventional loans to meet community credit needs that cannot be funded through bank or public loan sources. Each local NeighborWorks[®] organization is

responsible for setting strategy, raising funds and operating their program. Most provide homebuyer counseling, rehab monitoring, and targeted lending services that complement conventional lending activity.

The NeighborWorks[®] System integrates public and private support, leveraging federal funding to attract private resources. Private investors have viewed the NeighborWorks network as an increasingly sound investment; in fact, the typical NeighborWorks organization receives most of its funding from private sources and earned fees. Neighborhood Reinvestment does provide a critical financing vehicle to NeighborWorks[®] organizations in the form of equity capital grants for real-estate development and local revolving loan funds. The NeighborWorks[®] organizations, in turn, use these funds to draw private capital in a variety of ways, including equity and gap financing for home-purchase loans, including down payments and closing costs.

Loan recipients are typically underserved families. Seventy-one percent of loans made through NeighborWorks[®] revolving loan funds are made to very low- or low-income households, 53 percent to minority-headed households, and 43 percent to female-headed households. Loans carry a rate and term that the borrower can afford to pay back. The NeighborWorks[®] System is the only national nonprofit network with expertise in designing, originating and servicing small non-conventional loans to lower-income families. These loans help create first-time homebuyers, often prevent mortgage delinquencies, provide money for repairs, and help ensure accessibility for those with disabilities. The loans offered by local NeighborWorks[®] organizations provide a blanket of security for neighborhoods of modest means. By designing loans to fill the gap between the capacity of the borrowers and the parameters of conventional lenders, the NeighborWorks[®] organizations complete transactions that would not otherwise be made.

In Los Angeles, LA NHS originated \$72 million of lending activity for families of modest means in Fiscal Year 2002 alone. By utilizing public and private resources, LA NHS was able to assist nearly 15,000 families toward achieving their dream of homeownership.

The Need for Downpayment Assistance

Our experience in Los Angeles and throughout the national NeighborWorks[®] network is that one of the primary barriers to achieving the American Dream of Homeownership for low- and moderate-income people is the lack of accumulated wealth and disposable income.

Lower-income renters are at a disadvantage in accumulating cash to cover downpayment and closing costs. In order to accumulate wealth, households must consume less and save more or they must receive inheritances or cash gifts from relatives or other benefactors.

Lower-income households generally have to spend most of their small incomes for basic needs such as shelter, health care and food, leaving little for savings.

Aware that many families lack enough wealth to fund a conventional downpayment of, the mortgage industry has begun lowering downpayment requirements to 1 percent, or even less. While the mortgage industry is reaching out to families who are constrained from affording a home by wealth alone, lowering downpayment requirements may make income constraints worse by adding to the mortgage amount and increasing mortgage insurance premiums.

LA NHS EXPERIENCE WITH DOWNPAYMENT ASSISTANCE

LA NHS applies for and receives equity capital grants from Neighborhood Reinvestment Corporation. These grants are available to the entire NeighborWorks[®] network and are a critically important financing vehicle for revolving loan funds that support real-estate development and lending. NeighborWorks[®] organizations use these grants to provide the equity and gap financing necessary to make loans for home purchase, property purchase, rehabilitation and down payment assistance.

LA NHS helps low to moderate-income residents achieve the American Dream of homeownership by participating in state, county and city programs that benefit these potential homeowners by providing down payment assistance. LA NHS' Revolving Loan Fund (RLF) was developed to further assist very low to low-income borrowers who needed more assistance than these programs could provide. As local financial institutions merged and as our targeted communities became more underserved, LA NHS increased its direct lending efforts. This significantly increased the number of residents able to combine our funding with available public-sector assistance and conventional loan programs offered by lenders affiliated with Fannie Mae and Freddie Mac.

In our experience, low to moderate-income families who are able to receive down payment assistance, whether through public or private sector sources, have more capacity to achieve their dream of homeownership than do those who do not receive assistance. Given the limited resources, inability to build assets and lack of intergenerational transfers of wealth amongst these families, the funding provided for down payments and closing costs makes all the difference between success and failure. For example, during 2002, LA NHS worked in partnership with the City of Los Angeles to assist more than 300 low-income families to achieve homeownership utilizing a city subsidy program for down payment, closing costs and home rehabilitation. By providing up to \$75,000 as a second mortgage at zero percent for 30 years for eligible families, the City of Los Angeles quadrupled the number of families that had been assisted in prior years. As you can imagine, the enthusiasm of these triumphant new homeowners has a ripple effect that catalyzes other neighbors, friends and family members to succeed in their pursuit of homeownership as well, while becoming more active citizens who contribute to the betterment of Los Angeles.

According to a recent study cited in Fortune magazine (August 12, 2002), home equity appreciation has been the single most important driver of wealth creation in the United States over the past 30 years – outperforming the S&P 500 by 5% - even without accounting for the mortgage interest deduction. For low-income families, becoming an enlightened homeowner is perhaps the single most significant factor that will promote long-term economic stability. Subsequently, LA NHS has made homeownership and home preservation a priority as it assists families from a non-asset building position to one of building wealth.

A Comprehensive Homeownership Strategy

The NeighborWorks[®] Campaign for Home Ownership initiative is a joint effort of banks, insurance companies, secondary markets, government, the real estate community and others, coordinated by Neighborhood Reinvestment Corporation and involving more than 130 local community-based NeighborWorks[®] organizations to bring families of modest means into home ownership. The NeighborWorks[®] Campaign for Home Ownership has assisted over 65,000 low- to moderate-income families to purchase homes, educated more than 350,000 families, and generated over \$4.5 billion in investment.

Leaders of community-based organizations in the national NeighborWorks[®] network recognized that the conventional mortgage market could not fully meet the needs of their lower-income customers. By creating a system that reaches these customers, teaches them about home ownership, and prepares them to be owners, these nonprofits have not only been able to help lower-income families obtain the American Dream of Home Ownership, but have also done so in a way that reduces the risk of delinquency and foreclosure. This system, service marked as Full Cycle LendingSM, includes pre-purchase homebuyer education, flexible loan products, property services and post-purchase counseling.

Full Cycle LendingSM is a process that benefits all stakeholders in the homeownership arena. Residents can overcome hindrances to ownership as the process is demystified; they save for a down payment and they secure their home and mortgage. Lenders can invest with confidence about an owner's ability to repay the mortgage. Local government officials can take pride in watching neighborhoods change. More and more homeowners will stake a claim in their communities, enhancing the tax base and contributing to overall community stability and renewal.

The Steps of NeighborWorks Full-Cycle LendingSM



1. **Organization Partnership-Building.** The NeighborWorks[®] organization makes a commitment to the process by creating a partnership of residents, business and local government leaders. A plan for targeted community revitalization is put in place.
2. **Pre-purchase Homebuyer Education.** The homebuyer learns about the purchase process with a supportive organization that helps them clear up credit problems, find a home they want to buy, and coordinate the rehabilitation needs of the property.
3. **Flexible Loan Products.** Local lenders work with the NeighborWorks[®] organization to create mortgage products the customer can afford -- with features like lower down payments, downpayment assistance, and rehabilitation loans even when the total cost exceeds the value of the home. Property casualty insurance and mortgage insurance companies provide products that allow for the high loan-to-value ratios. The lender can hold the loans in portfolio or package and sell them to Freddie Mac or Fannie Mae's secondary markets. Neighborhood Housing Services of America purchases special-needs first mortgages as well as second- and third- mortgage rehabilitation loans. The secondary markets return funds to the lender, who recycles them by originating additional mortgages to the community.

4. **Property Services.** The NeighborWorks[®] organization inspects the property, offers technical assistance to the homebuyer and assists with the property's rehabilitation.
5. **Post-purchase Counseling.** The NeighborWorks[®] organization trains the new owners in home maintenance and budgeting, and supplies early intervention delinquency counseling so that defaults and foreclosures are avoided.
6. **Neighborhood Impact.** Homeowners gain a stake in their communities; lenders reach a significant market in which risk has been mitigated; the tax base increases; and the nonprofit partnership is one step closer to achieving its goal of neighborhood self-sufficiency. Everyone benefits.

NeighborWorks[®] Full-Cycle LendingSM is a means, not an end. As this comprehensive system is established, home-ownership rates among lower-income families rise, resulting in more stable communities with longer term residents, increased savings and civic involvement for individuals and families, and increased high school and college graduation rates for their children. By stimulating reinvestment in NeighborWorks[®] communities, Full-Cycle LendingSM is a powerful force that leads to a renaissance in lower-income neighborhoods across America.

Current Downpayment Assistance Efforts

LA NHS has utilized a variety of strategies with respect to down payment assistance for low to moderate-income families. Local and state government funding is critical in assisting our families to become homeowners by providing down payment, closing cost assistance, and home rehabilitation resources. In addition, some grant programs provide down payment assistance that does not have to be repaid. This is an essential element to encourage families to save their own funds, to lower loan-to-value ratios and potential default risk, as well as to lower monthly payments.

LA NHS utilizes Full Cycle LendingSM to implement its affordable homeownership programs, and offers the potential homebuyer down payment and closing cost assistance through matching grants, zero percent second and third mortgages, lease-to-purchase opportunities, below-market financing and employer-assisted housing initiatives.

Through the use of government subsidies and foundation grants, LA NHS has been able to encourage private corporations to participate in our homeownership efforts, as well as public housing authorities to assist families who may wish to move from Section 8 to homeownership. For example, LA NHS targets local employers to participate in providing down payment assistance to their employees as a part of their overall benefits program, and as a recruitment and retention tool. LA NHS has been successful in assisting public sector employees, such as firefighters, police officers, postal workers and teachers. While these efforts have been the result of assistance from the private sector,

union members, universities, hospitals, longshoremen and retail workers have benefited from LA NHS' efforts.

LA NHS provides on-site financial education through its "Lunch and Learn" program, as a tool to attract local employers, and then offers financial assistance to those workers who are eligible and graduate from the on-site classes. LA NHS utilizes government subsidy programs and more conventional financing for those families who are "more ready" to purchase a home, while those who have a lack of savings or credit challenges are encouraged to join the Individual Development Account (IDA) program, and to receive assistance from LA NHS through its Revolving Loan Fund. Through IDA, families can receive a 5:1 funding match (up to \$10,000 of their savings) for homeownership. Participating families receive 36 hours of financial education over the course of 12 months and also receive individual counseling and case management services. This attention and focus on the potential borrower ultimately produces a stronger, more prepared borrower in the long term and helps to reduce the risk of mortgage default. During its 18 year history, LA NHS has never experienced a foreclosure through its Revolving Loan Fund, and maintains a three percent or less delinquency rate.

As a member of the NeighborWorks[®] network, LA NHS has been participating in President Bush' minority homeownership initiative and the Sears American Dream Campaign. LA NHS' primary customers are typically 47 percent African-American, 45 percent Hispanic, 3 percent Asian, and 5 percent Caucasian and Other. Through the Sears American Dream Campaign, LA NHS was able to assist three families to purchase homes in late 2002 who would otherwise have not been able to afford their homes. All three families received down payment assistance from Sears and appliances to equip their new homes. They will receive ongoing counseling and the opportunity to participate in LA NHS home maintenance training courses.

An example of the importance of providing down payment assistance is notable through the experience of Naomi and Jae Beck. Naomi and Jae Beck, originally from Korea, were able to purchase a home through LA NHS. For the last 12 years Naomi has been a nurse at Shriner's Hospital, and Jae manages a garment factory. Neither ever expected they would be fortunate enough to buy a home. Then Naomi noticed a small ad in the *L.A. Times* for an introductory seminar being offered by LA NHS for potential first-time, lower-income homebuyers.

Naomi attended a full two-day homebuyer-education class and was told by NHS staff that her family's income and stable work history would qualify them for an affordable home loan.

The Becks began searching for a home and spotted one near their daughters' school. Although previous tenants left the home in terrible condition, the Becks were excited about the prospect of purchasing in this community. In January 2002, the Becks purchased a three-bedroom, one-and-a-half-bath home in Sunland, in the San Fernando

Valley. LA NHS financed the first mortgage, and the city of Los Angeles provided the Becks with a \$75,000 soft second mortgage through its "*HomeWorks!*" program. "*HomeWorks!*" encourages residents to purchase in neighborhoods targeted for revitalization by providing funding for renovations and bridging the affordability gap between what a house costs and what the purchaser can afford to pay. Of the \$75,000, \$25,000 was used to rehabilitate the home.

The Becks' monthly mortgage payment of \$1,018 is only \$68 more than their previous rent. LA NHS also monitored the rehabilitation of the Becks' home, which included a new kitchen, flooring, bathrooms, garage, windows and doors, paint and a fireplace.

Naomi is active in the Korean community and in February 2002, she hosted a press conference at which the Becks were interviewed by *The Korean Times*, Los Angeles and the Korean Television Enterprises, Ltd. Publicity from this event resulted in 600 Korean residents showing up for an introductory seminar on home ownership, and eventually more than 3,200 Korean families attended LA NHS' homebuyer education program. Naomi is now an active volunteer with LA NHS and refers customers on a frequent basis.

The Neighborhood Reinvestment Corporation estimates that the entire NeighborWorks[®] network will provide over \$10 million in downpayment and closing cost assistance in Fiscal Year 2003. The average interest rates of these loans is 5.34 percent, with some falling to as little as 1.88 percent, depending upon the borrower's ability to repay.

Lowered down payments can make homeownership possible for low-income buyers, but lenders rightly perceive these loans to be a higher risk than loans with lower loan-to-value ratios. The lender has less of a cushion in the event of a decline in house prices and the borrower has little to lose by walking away from property if the value of the home falls below that of the outstanding mortgage. As a result, the default costs of low-downpayment loans are often assumed to be higher than other loans, as evidenced by the performance of these loans in the past. To protect themselves, lenders therefore typically require mortgage insurance, which raises the monthly carrying costs of owning a home. As a result, the income constraint of homeownership can become a binding factor that keeps low-income families from being able to afford a home, regardless of downpayment assistance. In order to keep costs low for low-income homebuyers, perhaps mandating high quality pre-purchase counseling for lower-income homebuyers with little or no downpayment could allow for a reduction in mortgage insurance.

LA NHS and all other community development corporations would support an increase in resources that reach local communities that desperately need funding. However, offering downpayment assistance without the benefit of pre-purchase homebuyer education would be a tremendous mistake and a potential waste of money. Homebuyer education is the key to keeping new homeowners in their homes.

Conclusion and Summary

Let me close by thanking the Subcommittee for the opportunity to speak about the work of Los Angeles Neighborhood Housing Services and the broader NeighborWorks[®] Network. The addition of a national downpayment assistance pool would tremendously assist the work of the Los Angeles Neighborhood Housing Services and the entire NeighborWorks[®] network. However, merely creating homeowners is not sufficient to stabilize the communities I work in as well as the 2,300 communities served by the NeighborWorks[®] network. Through pre- and post-purchase education combined with financial assistance, the Los Angeles Neighborhood Housing Services and the NeighborWorks[®] network will continue to create sustainable homeowners who will work to revitalize this nation's communities.